

Assembly Bill 2366 (Dickerson)

Conflicts: retail sales exception in small jurisdictions

Version: As introduced, February 21, 2002

Status: Assembly Elections Committee

Existing Law and Regulations

Government Code Section 87103 prohibits a public official from making, participating in making, or using his or her governmental position to influence a decision in which he or she has a financial interest. A financial interest includes sources of income of \$500 or more received by a public official. This amount was increased from \$250 in 2000 by Commission-sponsored legislation.

Under existing law, an exception to this basic conflict-of-interest disqualification rule is available for income derived from retail sales¹ provided that: 1) retail customers of the business are 10% or more of a jurisdiction's population; and 2) the amount of income received from a retail customer is indistinguishable from its other retail customers. This "indistinguishable" test is set out in Commission regulation at less than one-tenth of one percent.²

Summary of Proposed Bill

AB 2366 would eliminate the "indistinguishable income" prong of this exception for jurisdictions with populations below 10,000. As a result, a public official who is a business person engaged in the retail sales in one of these jurisdictions would be permitted to vote on matters in which they currently have a financial interest, even if 50% of their business revenues were derived from a source who is the subject of the governmental decision in question.

This bill does this by adding the following subdivision to Government Code Section 87103.5:

¹ Government Code § 87103.5 provides: "Notwithstanding subdivision (c) of Section 87103, a retail customer of a business entity engaged in retail sales of goods or services to the public generally is not a source of income to an official who owns a 10-percent or greater interest in the entity if the retail customers of the business entity constitute a significant segment of the public generally, and the amount of income received by the business entity from the customer is not distinguishable from the amount of income received from its other retail customers."

² Regulation 18703.5 was renumbered 18707.5 during Phase 2 of the Conflict-of-Interest Regulatory Improvement Project and provides as follows:

(a) For purposes of Government Code Section 87103.5, the retail customers of a business entity constitute a significant segment of the public generally if either of the following is true:

(1) The retail customers of the business entity during the preceding 12 months are sufficient in number to equal 10 percent or more of the population or households of the jurisdiction; or

(2) The retail customers of the business entity during the preceding 12 months number at least ten thousand.

(b) For purposes of Government Code Section 87103.5, the amount of income received by a business entity from a retail customer is not distinguishable from the amount of income received from its other retail customers if the amount spent by the customer in question during the preceding 12 months is less than one-tenth of 1 percent of the gross sales revenues of the retail business entity for the preceding year.

(b) Notwithstanding subdivision (c) of Section 87103, in a jurisdiction with a population of 10,000 or less, a retail customer of a business entity engaged in retail sales of goods or services to the public generally is not a source of income to an official of that jurisdiction who owns a 10-percent or greater interest in the entity if the retail customers of the business entity constitute a significant segment of the public generally.

History of Bill

This is an author-sponsored bill brought to Assembly Member Dickerson's attention by a constituent, Siskiyou County Superintendent of Schools Barbara Dillman. Superintendent Dillman says that one of her county board of education members owns a card-lock gas station in Seiad, a small community in remote northwestern Siskiyou County. Her board attorney has opined that it would be a conflict of interest for a school nurse, speech therapist or other county school employees to purchase gas from the board member's gas station—one of two card-lock stations in the area in question. The superintendent says that she is concerned about county employees running out of gas in this remote area.

In addition, the superintendent provides further background about a conflict situation in which she was the disqualifying source of income. This situation was highlighted in Advice Letters A-93-292 and I-93-324, and was the subject of an enforcement action (see below).

In 1993, Superintendent Dillman's husband was attempting to build a brewery in the City of Weed. Ordinance revisions were necessary in order for the project to move forward. City Council Member Amelia Borcalli, who supported the project, owned one of two hardware stores in Weed. Mr. Dillman was a customer of Borcalli's hardware store with a level of 1992 patronage characterized in the following paragraph.³ Borcalli requested advice from the FPPC on whether she could vote on zoning changes necessary for Dillman to build the brewery.

Hardware Store Gross Revenues	Dillman's Purchases	Dillman's Purchases as a % of Hardware Store's Total Revenues
\$322,523	\$2,275	.71%

Using the criteria outlined in Regulation 18707.5, the FPPC found that Borcalli had a financial interest in Dillman because his contribution to the hardware store's revenues was .71% of the store's total revenues, thus exceeding the .1% threshold. The FPPC advised Council Member Borcalli in an August 20, 1993 advice letter that she would not be able to participate in the city council decision regarding the Dillman project.

Against the advice of the city attorney, Council Member Borcalli voted on the ordinance changes on August 17, 1993. An Enforcement action was subsequently brought by the Commission against Council Member Borcalli and she was fined \$2,500 for violating section 87100.⁴

³ Based on Amelia Borcalli's supplemental request for advice dated August 9, 1993.

⁴ Government Code § 87100. No public official at any level of state or local government shall make, participate in making or in any way attempt to use his official position to influence a governmental decision in which he knows or has reason to know he has a financial interest.

Background of the Law

The League of California Cities proposed the concept for Section 87103.5 at the FPPC meeting in December, 1983. The Commission voted to sponsor this bill in February, 1984, and the bill became law later that year. The purpose for Section 87103.5 was to alleviate conflict-of-interest situations in small, rural jurisdictions where a retail business owner has a large portion of the population as customers, making them sources of income and requiring disqualification as to decisions affecting any one of them.

The Commission considered regulation 18707.5 after receiving several expressions of concern about the application of Section 87103.5 in the context of family-owned hardware stores in urban areas. The Commission adopted this regulation at its September 8, 1988 meeting and it became effective December 21, 1988. It provides guidance “as to what constitutes a significant segment of the public in the situation of a retail store” and “for determining whether a given customer spends an amount which is not distinguishable from the retail business’ other customers.”⁵ At the September 8, 1988 meeting, there was significant debate focusing on whether the distinguishable threshold in 18703.5(b) should be one-tenth of one percent or one-quarter of one percent. It is worth noting that, even at the higher one-quarter of one- percent threshold discussed by the Commission, Council Member Borcalli would have been disqualified.

Discussion and Policy Considerations

Contrary to Basic Conflict Prohibitions. This proposal would allow public officials in jurisdictions with 10,000 or fewer people to participate in governmental decisions despite sometimes considerable financial interests based only on the criterion that they sell to a significant segment (10% or more) of the population. This means, in the case of *In re: Borcalli*, that Ms. Borcalli’s hardware store could have received 50%, or even 80% of its income from Mr. Dillman and the councilwoman still would have been allowed to participate in a decision related to the Dillman brewery project. Even using the actual facts of the case, the \$2,200 Borcalli’s hardware received was an amount likely to create bias or an appearance of bias.

Likewise, the notion that a business owned by a county board member should be allowed to benefit financially sales to the county office of education is contrary to the very basis of the Act’s conflict-of-interest prohibitions. Even if the amount of money is nominal, the public appearance that would be created by such apparent self-dealing would damage the integrity of governmental agencies. Finally, even if an exception like the one proposed in this bill were created in the Act, the criminal or other penalties of Government Code 1090 might still apply.

Obvious Alternatives to a Change in Law. Each of the factual situations used in support of the need for this bill offers very clear alternatives to changing the law. With regard to the current issue with the Siskiyou County Office of Education, the superintendent relates that there are two

⁵ See Notice of Proposed Rulemaking published July 29, 1988.

card-lock gas stations in the area in question. Her letter informs that the county school board member owns one, so presumably employees could purchase fuel from the other station, or from other non-card-lock stations in the area. In any event, the area in question is just 55 miles from Yreka, the county seat: employees could simply fuel up at another station before traveling to the area in question. Other alternatives, such as a county road department fueling station and gas stations in the neighboring towns of Happy Camp and Etna, also exist.

Similarly, the facts in *In re: Borcalli* make clear that an alternative to the change proposed in this bill existed. Had Mr. Dillman simply shifted his purchases from Ms. Borcalli's hardware store to the other local hardware store mentioned in Ms. Borcalli's letter requesting advice, the councilwoman could have voted on the Dillman brewery project just twelve months later. In fact, Advice Letter A-93-292 informed Borcalli, "Once twelve months have elapsed from the date of . . . payments aggregating \$250 or more, you will no longer have an economic interest in Mr. Dillman and may participate in decisions affecting Mr. Dillman." [Emphasis in original.] In addition, a second member of the council was prevented from voting in the 2-3 outcome because he was an attorney retained by Mr. Dillman—a conflict which could have been easily avoided.

In *In re: Borcalli*, Regulation 18707.5 worked the way it was intended, by preventing a public official with a financial interest in a decision from participating in that decision. In 1993 the FPPC advice letter found Borcalli to have a financial interest in Mr. Dillman as a source of income; she should have recused herself from participating in decisions relating to the Dillman brewery project. This principle has been in place for 14 years, and this particular situation demonstrates its importance in eliminating potential conflicts-of-interest.

Commission to Review Regulation Later this Year. In addition to the above concerns, this proposal is inappropriate at this time as the Commission is scheduled to review Regulation 18707.3, the public generally exception applicable to small jurisdictions, later this year to address other concerns raised by the small cities group in the League of California Cities. Interested persons meetings are expected in July and pre-notice discussion will be before the Commission in September.

Staff Recommendation: Oppose.